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Before the
Federal Communications Commission
Washington, D.C. 20554

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JUL 13 1992

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of)

Review of the Commission's)
Regulations and Policies)
Affecting Investment)
in the Broadcast Industry)

MM Docket No. 92-51

**ORIGINAL
FILE**

TO: The Commission

**REPLY COMMENTS OF THE
NATIONAL ASSOCIATION OF BROADCASTERS**

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Summary

The National Association of Broadcasters (NAB) welcomes the Commission's inquiry into regulatory changes which will enhance broadcasters' opportunities to obtain financing for station acquisitions and improvements in facilities. With the decline in bank financing of broadcast transactions, it is increasingly important that the Commission remove any regulatory impediments to broadcast financing that do not serve an articulable public purpose.

NAB agrees with the parties supporting the Commission's proposals to double the attribution benchmarks for active and passive investors to ten and 20 percent, respectively. Greater flexibility in attribution standards may permit the creation of new investment vehicles for broadcast stations, permitting large numbers of investors to participate in the broadcasting industry. The Commission properly recognizes that holders of minority interests in licensees who have no management position will not be able to exercise any meaningful control over stations. NAB also supports the Commission's proposal to permit new types of passive institutional investors to qualify for the higher attribution benchmark, and NAB agrees with the parties who suggested that any institutional investor be permitted to own up to 20 percent if its interest is entirely passive.

The Commission is also correct in proposing changes in its insulation criteria for limited partners which are inconsistent with federal and state securities laws. The very limited role which limited partners may have in selecting general partners under such securities laws can hardly be equated with day-to-day control over a station, and

limited partners who have no greater interest should not be deemed to have an attributable interest in stations in which the partnership invests. The Commission should also change its treatment of participants in widely held limited partnerships to treat those interests as it does ownership of corporate stock for attribution purposes. The regulatory treatment of investments in broadcast stations should turn on whether the investor is in a position to exercise control, not on the technical form of the investment.

The Commission should not, however, change its policies to permit lenders to obtain security or reversionary interests in station licenses. Given the statutory bar to any property interest in licenses and the uncertain state of the treatment of broadcast assets under the bankruptcy laws, it is far from clear what effect, if any, the Commission's acceptance of security or reversionary interests would have.

On the other hand, NAB believes that affording lenders such interests would reduce licensees' independence from control by lenders who may not have been approved by the Commission. Lenders now have a strong incentive to work out problem broadcast loans to the benefit of the public, the broadcaster, and the lender. Permitting enhanced security or reversionary interests might shift the balance to favor earlier foreclosure, or enable lenders to place greater pressure on stations. Particularly in the absence of any meaningful assurance that new security interests would increase the amount of capital available to the broadcasting industry, the Commission should decline to overturn its longstanding policies concerning security and reversionary interests in licenses.

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The National Association of Broadcasters (NAB)^{1/} submits these comments in reply to the comments submitted in response to the Commission's *Notice of Proposed Rule Making and Notice of Inquiry*. NAB supports the Commission's efforts to improve broadcasters' opportunities to obtain financing for station acquisitions and improvements, such as the capital that will be needed to convert existing stations to High Definition Television or Digital Audio Broadcasting.

While the Commission should take steps to improve access to capital for broadcasters, it should avoid actions which may substantially change the principles of licensee responsibility. Therefore, while the Commission should expand the range of options for investment in broadcast stations, NAB opposes the proposal that the

^{1/} NAB is a nonprofit, incorporated association of radio and television broadcast stations and networks. NAB serves and represents America's radio and television stations and all the major networks.

Commission permit banks and other creditors to obtain security or reversionary interests in broadcast licenses.

The need for innovation in the broadcast financing environment is striking. In 1989, banks supplied 2.2 billion dollars of new financing for broadcast stations. Two years later, the amount of new bank financing had collapsed to only 191 million dollars.^{2/} A significant reason for this breakdown was the adoption by federal banking regulators of regulations concerning financing of Highly Leveraged Transactions (HLTs), regulations which had a particularly onerous effect on broadcast lending since the HLT definition did not take account of the value represented by a broadcast license. As the Commission recognizes, the broadcasting industry played a leading role in convincing the banking regulators to abandon their HLT regulations as of June 30.^{3/} NAB also recently filed comments supporting proposals of the Securities and Exchange Commission to simplify access to capital markets for smaller companies desiring to issue debt or equity securities, another way in which broadcasters may seek investment capital.^{4/}

The importance of a vibrant capital market for the broadcasting industry can hardly be overstated. In the absence of readily available sources of capital, new

^{2/} Paul Kagan Associates, Inc., *Broadcast Banker/Broker*, No. 85, at 3 (May 31, 1991).

^{3/} Notice ¶ 1 n. 1; see *The Regulatory Definition of Highly Leveraged Transactions*, 57 Fed. Reg. 5040 (Feb. 11, 1992).

^{4/} *Small Business Initiatives*, SEC File No. S7-4-92, 57 Fed. Reg. 9768 (Mar. 20, 1992); Comments of the National Association of Broadcasters (filed June 18, 1992).

entrants will be foreclosed from the broadcasting industry. Without financing, the market for existing stations will diminish and the value of stations will decline precipitously. A recent survey of industry values conducted by *Broadcasting* magazine indicates that this has already occurred; it found that the asset value of the broadcasting industry was down by almost one third, largely due to the absence of financing for acquisitions.^{5/} An industry characterized by declining values will find it increasingly impossible to finance improvements in equipment and services, resulting in a deterioration of service to the public. Further, licensees who desire to retire or otherwise dispose of stations will experience great difficulty in finding available buyers, forcing them to continue operating facilities contrary to their wishes. As the Commission reconsiders its ownership rules to permit entities to own or control a greater number of stations,^{6/} broadcasters will also require access to capital to take advantage of the new ownership options. It is in this context that NAB addresses the proposals put forward by the Commission.

I. The Commission Should Modify its Attribution Rules to Permit Increased Investment in Broadcast Stations

The Commission presently deems a holder of five percent of the voting stock of a licensee (or a corporation controlling a licensee) to have an attributable interest in

^{5/} "Valuing the Big Three: Telcos Get Bigger," *Broadcasting*, Aug. 19, 1991, at 19.

^{6/} *Review of the Commission's Regulations Governing Television Broadcasting*, MM Dkt. No. 91-221 (rel. June 12, 1992); *Revision of Radio Rules and Policies*, 7 FCC Rcd. 2755 (1992), *pets. for recon. pending*.

the license, restricting the other broadcast investments which the stockholder can make and subjecting the stockholder to the Commission's reporting requirements. For a narrowly defined class of passive institutional investors, the Commission now permits holdings of up to ten percent of a licensee's voting stock before the investor's interest is deemed attributable. Only limited partnership interests which meet detailed insulation requirements are deemed to be non-attributable, even if the interest held by the limited partner is far less than the attribution benchmark for stock.

NAB agrees with the commenting parties supporting the Commission's proposal to relax these attribution rules. Although the elimination of the HLT regulations should improve the climate for debt financing of broadcast stations, it is probably unrealistic to suppose that the banking climate, particularly for broadcast stations, will sufficiently recover in the near future to meet the capital needs of the broadcasting industry. Broadcasters instead will be looking for new sources of equity capital as a way of entering the market, acquiring new stations, or improving their facilities. Changing the attribution rules will permit new forms of investment in broadcast stations. As described in comments of ML Media Partners, L.P., the present rules restrict the types of investors who can take minority positions in broadcast stations, or else require such investors to obtain waivers before applications in which they are a participant can be granted. The comments of the Prudential Insurance Company (Comments at 4-6) demonstrate that uncertainty about the application of the Commission's ownership rules to passive investors deters investment as the cost of ensuring regulatory compliance, and the potential risk to the

investment if the Commission were subsequently to determine that its rules had been violated, increase. More flexible attribution standards may encourage the creation of new investment vehicles by which interests in broadcast groups and stations can be shared among a great number of investors without raising multiple ownership issues or creating difficult disclosure obligations.

NAB, therefore, supports the Commission's proposed doubling of the attribution standards to ten percent for active investors. As the Commission recognizes (*Notice ¶ 9 n.11*), officers and directors of a licensee will continue to be deemed to have an attributable interest, regardless of the level of their ownership interest. This will in almost all instances prevent an investor who has active control over a licensee's operation from avoiding the multiple ownership rules through non-attributable ownership positions in stations which the investor could not otherwise control. Few investors bent on controlling a group of stations will be content with owning only a small minority share without any opportunity to serve as an officer or director.^{7/} The Commission should be confident that an owner of ten percent or less of a licensee, and who has no other interest in the station, will not be in a position to exercise control over the station and thus implicate the multiple ownership rules.

Similarly, NAB supports the proposed increase of the attribution benchmark for passive investors to 20 percent. NAB agrees with the Commission that the

^{7/} Since the Commission will continue to be informed of the broadcast-related interests of all directors and officers of licensees and companies controlling licensees, it will have adequate means to determine whether an investor might be attempting to circumvent the rules through the use of designees. No other rules are needed to deal with this unlikely scenario.

speculative possibilities of an institutional investor influencing a licensee through voting or trading its stock is too remote to be considered as equivalent to day-to-day control over the licensee, particularly as the Commission intends to continue to require that licensees certify that passive investors have not sought to exercise control over their affairs.

The interests represented by passive institutional investors provides assurance that they will not exercise control over licensees. Institutional investors are not in the business of operating companies, but instead of increasing the income or capital of their investors. Their concerns are met by identifying companies with competent management and then allowing those managers, who are subject to the attribution rules, to operate stations to increase the value for investors. *See Comments of A.H. Belo Corporation, et al.*

The Commission also proposes to add Small Business and Minority Small Business Investment Companies to the class of institutional investors entitled to the higher attribution benchmark. NAB supports these proposals as a means of broadening the class of potential investors in broadcast companies, in particular as a means of increasing the opportunities for minority ownership of stations. *See Comments of the Minority Broadcast Investment Corporation.* We note that some commenting parties suggested that the Commission go further and permit any institutional investment entity to take advantage of the passive investment attribution limit. *See Comments of Koteen & Naftalin.* NAB believes that these proposals merit serious consideration by the Commission. The Commission recognizes that passive investors should be

accorded different attribution treatment since they waive any right to control a licensee's affairs. The particular form which such an investment entity may take may vary depending on tax considerations and state laws relevant to the investment objectives sought to be met by the entity's creators. It is not clear whether any public purpose is served by varying the regulatory treatment of institutional investment vehicles depending on particulars of their form that have no likely effect on their operations.

The Commission also asked for comments on changes in its standards for attributing control of licensees to limited partners, particularly in connection with widely held limited partnerships. NAB agrees that conflicts between the Commission's insulation criteria for limited partners and federal and state securities laws should be eliminated wherever possible, again to promote the greatest possible number of avenues for investment in broadcast stations. Permitting limited partners to vote on the admission or removal of general partners will not place such limited partners in a position to control the day-to-day affairs of licensees in which the limited partnership invests. General partners would continue, of course, to be deemed to have an attributable interest in licensees in which the partnership invests. Insisting on insulation criteria which are at odds with other regulatory requirements or which are inconsistent with business practices merely reduces the potential for investment in broadcasting, or requires investors and the Commission to expend resources on repeated requests for waivers.

Further, the Commission should end the presumption that partnership interests, no matter how small, bespeak control over a licensee. Widely held partnerships which may include thousands of investors are akin to a corporate owner and do not resemble small partnerships composed of persons who control or operate a station. Limited partners whose interests are under ten percent of a partnership's assets should be deemed non-attributable in the absence of some other indicia of control, just as similar stock interests will be treated under the Commission's proposed rules. *See* Comments of A.H. Belo Corporation, *et al.*; Comments of The Prudential Insurance Company; Comments of ML Media Partners, L.P.

II. The Commission Should Not Permit Security or Reversionary Interests in Licenses

The Commission asked for comments on two requests that the Commission declare that lenders to broadcast stations may obtain security interests or reversionary interests in station licenses. As the Commission noted (*Notice* ¶ 21 n.30), the courts are divided on the issue of the treatment of broadcast stations' assets in bankruptcy proceedings. Given the absolute statutory bar on anyone obtaining an ownership interest in the spectrum, 47 U.S.C. §§ 301, 304, 309(h)(1), it is not clear whether any action which the Commission could take would resolve these disputes, either for existing or future agreements.

NAB believes that the issue of secured lenders' positions in the distribution of the assets of a bankrupt station will not necessarily turn on the Commission's views of security interests as none of the decisions to date appears to have considered the

question of whether a senior lender should be afforded a "going concern" valuation even if it does not have a complete security interest in the broadcast license. Given the uncertain state of the bankruptcy law, the Commission should not rest its decision on any anticipated effects of granting security or reversionary interests in liquidation proceedings.^{8/}

The question for the Commission, therefore, is more one of the relationship between licensees and their lenders and between lenders and the Commission. NAB believes that the policy questions raised by the Commission in connection with security and reversionary interests (*Notice* ¶ 23) are generally well taken. Notably, the lenders commenting in this proceeding have not provided any assurances that a change in the Commission's policies will result in increased capital being made available for broadcast loans, preferring instead to predict that lending will dry up if the Commission does not approve new security measures.

Such predictions, while hardly surprising, must be viewed with some skepticism by the Commission. The difficulty in obtaining a completely secure position with respect to broadcast loans is hardly new. The Commission has always barred agreements which granted lenders security interests in licenses or reversionary interests. Despite this, loans have been made to broadcasters, based on an assessment

^{8/} Proponents of security interests (*E.g.*, Comments of Media Venture Partners) argue that such interests would be limited to whatever right the licensee possesses, subject to Commission supervision of any change in control. It is not clear how such an interest differs from interests which the Commission now permits, such as stock pledges in corporate licensees, or what practical effect such a new form of interest would have.

of stations' underlying value and of the borrower's business acumen. While some lenders may have extended credit in the past based only on an assumption that their interests would be fully secured regardless of the transaction's underlying merit, the lending environment which permitted such transactions has disappeared.^{2/}

Instead, NAB believes that acceptance of greater security interests or reversionary interests would diminish the independent control of station licensees. Lenders with reversionary interests or perfected security interests would have far less hesitation in foreclosing on stations which they feared were not performing up to expectations than lenders do now. Lenders presently have a strong incentive to work out nonperforming broadcast loans, rather than face the complex process of seeking Commission permission to take control of a licensee. Broadcasters may feel compelled, if lenders obtain new rights in their licenses, to hew to lenders' demands concerning station operations, effectively ceding control over the station to persons or institutions who have not been approved by the Commission. Reversionary interests in particular would appear to create problems with unauthorized control as the former licensee may have strong views on how a station should be operated.

^{2/} Similarly, the Commission should not uncritically accept that argument raised by the Motion Picture Association that program suppliers and other unsecured creditors require assurances that senior lenders will not be given first preference in any proceeds of a station sale. Unlike other creditors, program suppliers are able to reclaim their goods in the event of a station failure and offer them to other stations in the market, sometimes at a higher price. Particularly since broadcasters are the only mass market available for broadcast programming, there is no reason for the Commission to take any steps to ensure a better position in liquidation proceedings for such unsecured creditors than they may have under existing law.

Although NAB believes that the Commission should not create any unnecessary impediments to new means for financing broadcast stations, the Commission must adhere to principles which form the basis of its licensing system. The Commission has an established policy of cooperating with receivers and bankruptcy courts to ensure that lenders are not deprived of the security for their loans. *See LaRose v. FCC*, 494 F.2d 1145 (D.C. Cir. 1974). That policy, however, should not extend to granting lenders the opportunity to exercise control over stations which the Commission has granted exclusively to licensees.

Conclusion

NAB welcomes the Commission's interest in reducing the regulatory barriers to increased investment in the broadcast industry. Coupled with the removal of HLT restrictions by the banking agencies and proposed simplified procedures for public offerings by the SEC, the raising of the Commission's attribution benchmarks will create significant new opportunities for broadcast entrepreneurs to obtain financing for

new or improved stations. The Commission should not, however, modify its positions concerning security and reversionary interests in broadcast licenses.

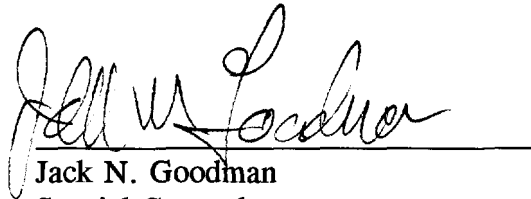
Respectfully submitted,

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A handwritten signature in black ink, appearing to read 'H. Baumann', written over a horizontal line.

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Executive Vice President
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A handwritten signature in black ink, appearing to read 'Jack N. Goodman', written over a horizontal line.

Jack N. Goodman
Special Counsel

July 13, 1992